Special Papers and Research Reports

Congregational Endowment Funds

Empowering the Vision of God's Coming Kingdom

by
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Resources for people who care about congregations.

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CONGREGATIONAL ENDOWMENT FUNDS: EMPOWERING THE VISION OF GOD'S COMING KINGDOM

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Congregational endowment funds provide financial resources for continuing and expanding congregational ministries into the future. The vision of the future toward which God calls a congregation forms the basis for mission. Endowment money provides the financial power to move in mission toward the vision of God's coming kingdom.

I. Why have an endowment fund?

An endowment fund can serve several purposes.

1. It can provide funding for special ministries, or for improvements to the building or property, that could not be financed from the operating budget. A radio ministry, special youth program, special equipment for educational ministry, or new musical instruments to aid in worship are a few such items.

2. Given the shrinking financial resources going to congregational operating budgets, it may be useful to allocate income from the endowment fund to help pay the bills. Traditionally this view has been considered a kind of heresy. Endowment income is almost exclusively used for special projects. But it may be time for change. The issue of mission versus survival is crucial. Mission must drive the use of the fund.

3. It gives people who want to support ministry beyond their life times an opportunity to do so. The gift represents the donor. It is a gift that keeps on giving.

II. The importance of mission.

Movement toward the realization of God's kingdom guides the purpose of the fund. It is mission driven. The congregation needs a clear sense of its mission. Spending priorities need to be set accordingly.

Lack of a mission focus results in, or is caused by, a survival mentality. Self serving rather than God serving guides the congregational agenda. Conflict results or, if it already exists, is intensified.

Please note: If a congregation is experiencing conflict, an endowment fund is one more excuse to fight.

III. How to start an endowment fund.

A. Determine the organizational structure of the fund: Either as a committee of the congregation, or as a separate corporation.

1. The advantage of organizing the fund as a committee is that it is established by adopting a by-law to the congregational constitution, a relatively easy process. The disadvantage to the committee form is that it is easy to borrow, or tempting to borrow, from the fund should operating funds be short. To borrow defeats the concept of the fund, that the principal remains intact and only income is used to support special ministries.

2. The advantage of the corporate structure is that it eliminates the ability to borrow from principal. The disadvantage is that a new entity separate from the congregation is created. This requires the process of forming a new corporation, filing for nonprofit corporation status with the IRS (note: the 501 c 3 category of nonprofit corporation needs to be used in order for contributions to be tax deductible.), and a separate board of trustees with special reporting requirements needs to be established. It also entails legal fees.

   Most congregations use the committee format and safe guards into the by-laws to prevent borrowing.

B. Establish the purpose of the fund.

As indicated in section I., the fund can and usually does serve the purpose of providing financial resources for ministries and capital or equipment needs that could not be funded from the operating budget. Some congregations also designate monies from their endowment funds to be used to assist other congregations, special ministries outside the congregation, or community service programs. The potential for using income from the fund to support the operating budget (for mission, not survival) should be considered at this point.

The purpose of the fund and the categories of needs it may fund should be clearly stated as the first item in the by-law or articles of incorporation. Categories should be stated in terms sufficiently broad as to not be restricting when it comes time to determine funding requests.

C. Elect the governing board for the fund.

1. Determine the number of members for the board. For newly established fund a five member board should be adequate. The (a) pastor should be included. The larger the congregation and the larger the fund the larger the board might be.

2. Determine what categories of members should be on the board: ie. pastor, members of congregational governing body, members at large. Use the mix of members that best serves the needs of the congregation and the fund.

3. Set the terms of office. Three year terms are suggested. Make sure the terms are staggered so the entire board membership does not change at the same time. Continuity is very important.

4. Consider what potential board members might be selected because of special knowlegdge or skills they might bring. Stock brokers, attorneys, accountants, insurance agents, and financial planners would be valuable people to have on the board.

   Two concerns for caution require attention:
   A. Do not let technical and financial accumulation concerns overshadow the focus on mission which is why the fund exists.
   B. Do not depend so heavily on the expertise of one specialist that if that person is no longer around the rest of board members are left not knowing how to handle the fund. People do die or move.

5. Determine what authority the board will have. How much leeway does the board have in making investment and spending decisions. Are there limits to how much money the board can allocate to a need before a congregational vote is required.

6. Decide how often the board will meet. Meetings may be quarterly when the fund is first established and more frequent as the fund grows. The situation of each congregation should serve as guide.

7. Establish reporting procedures. Should the board report to the congregation on an annual, semi-annual, or quarterly basis. Included in the report should be gifts received, needs funded since the last report, and the net asset value of the fund.

IV. Marketing the fund.

A. Once the fund is established, a brochure should be written and provided to members and other potential donors. It should describe the purpose of the fund, how people may donate to the fund, and how both donors and the congregation benefits from the gifts. The brochure should reflect a theology of stewardship consistent with the denominational affiliation of the congregation.

B. The congregational newsletter can serve to remind people of the fund. It is important to keep the fund in front of people. Information about the fund and how it furthers ministries may be included. A single sentence reminding members that the fund exists can also serve the purpose.

C. Educating members about the fund can take several approaches. Short temple talks can be given during a worship service or at meetings of congregational organizations. Special programs on topics such as estate planning are natural contexts for the discussion of charitable giving and the congregational endowment fund. Newsletter articles also serve an educational purpose.

D. The solicitation of gifts must be seen as much more than just a transfer of money from the donor to the church. The gift represents the donor's self in the support of the mission of the church. Donors are investing themselves in the financial empowerment of mission with gifts that keep on giving.

The asking process is really providing a way for the potential donor to accomplish the donor's goal. If the donor has supported the mission of the church during this lifetime, the donor may well be excited about the possibility of providing a gift to keep on funding ministry after the donor's death. The solicitor helps the donor to see the possibilities.

The solicitor who will approach potential donors should be someone who already knows them. An established relationship is helpful since relationships are important, especially in asking for larger gifts. It is good to remember that people give to people.

E. The relationship of the endowment fund to memorial and restricted funds should be clear. It is important that people know what money goes where and to be used for what purpose.

F. Gifts of appreciated assets, such as stocks, can eliminate capital gains taxes for the donor. The potential benefits should be used where appropriate as a marketing tool.

The following three sections deal with ways to give to the endowment fund beyond the cash gift.

V. Wills

Giving by means of a bequest is easy. A portion of the donor's estate is designated for the congregation. It is best to establish the amount of the gift as a percentage of the estate rather than as a stated dollar amount. The value of an estate can and does change over time. Designating fixed dollar amounts could result in some beneficiaries being excluded from estate proceeds because there is no money left.

A new will can have the bequest written into it. An existing will can have the gift included b way of a codicil.

VI. Planned gifts (also termed deferred giving) are gifts given now. The principal amount of the gift goes to the congregation at a future date. The donor receives a stream of income from the gift and a tax deduction. The donor has the satisfaction of making the gift while alive, still having income on which to live, and saving on taxes.

Planned gifts include:

1. Charitable Remainder Trust. An irrevocable transfer of assets is made to the trust. If appreciated assets are used the capital gains tax is eliminated. The trust pays the donor income for life or for a specific term such as ten years. The payment is a fixed percent of the fair market value of trust assets and changes annually. Assuming the percent of payout to the donor (must be at least 5% by law) es less than the trust earns, the amount of income would increase each year providing a hedge against inflation. The donor receives an immediate income tax deduction. The trust principal goes to the congregation at the end of the trust period.

2. Charitable Remainder Annuity Trust. It pays a fixed dollar amount to the donor based on the value of the assets as of the date of the gift. The amount of payout remains the same regardless of market conditions. Otherwise it is similar to the Charitable Remainder Trust.

3. Charitable Gift Annuity. No trust is involved. It is an outright gift to the congregation which agrees to pay the donor a fixed amount each year. There is an immediate tax deduction. Payment of income to the donor may be delayed if the donor wishes, increasing the amount of the principal on which the payment would be calculated. Part of each payment is tax deductible. It works like an immediate annuity purchased from an insurance company.

4. Charitable Lead Trust. It provides income to the congregation for the term of the trust. The principal of the trust passes to the person designated by the donor at the end of the trust.

5. A Home as a Gift. In this arrangement the home is donated to the congregation. The donor has the right to use the home for life, or until other living arrangements are made. The donor receives an income tax deduction immediately and a reduction in estate taxes at death.

These planned gift arrangements are attractive for those who want to make a donation, but who need income for living or need to continue living in their home. There is a lot of marketing potential in these gifts that is never tapped.

A trustee/custodial financial institution is usually required to administer these gifts. Fees are charged based on the size of the gift on a percentage basis.

Care must be taken in establishing planned gifts to avoid inadvertent tax liabilities. Caution: Use attorneys or accountants who have special competence in charitable giving.

Planned gifts are generally better suited to people at least sixty years of age. The percent of payout increases with age, depending on the gift arrangement.

VII. Life Insurance.

Life insurance can be given as a gift either by transferring ownership of an existing policy to the congregation and making the congregation also the beneficiary, or by purchasing a new policy with the congregation as owner and beneficiary. A new policy is ideally suited to a person who wants to make a larger gift, that is possible by death benefit, than the donor could make in cash.

Caution: If the donor has any incidence of ownership in the policy, such as the ability to change beneficiaries, the tax deduction is lost.

The tax deduction for an existing policy is usually the amount of the cash surrender value on the date of the gift.

A new policy as a gift may be paid in two ways. The donor can pay the premium amount to the congregation which in turn pays the insurance company, or the donor can pay the premium directly to the insurer. The donor then receives a statement of donation for the gift. The former payment arrangement is cleaner for tax purposes.

Another use for life insurance in the gift process is wealth replacement. Assets are donated to the congregation and replaced in the donor's estate with life insurance. This arrangement can be beneficial where appreciated assets would trigger a large capital gains tax if liquidated.

Benefits accrue to the donor, heirs, and the congregation. Caution: Be sure to use a life insurance agent who knows the technicalities of charitable life insurance. The concept works as follows:

-The life insurance policy serving as wealth replacement in the donor's estate must be owned by a life insurance trust, or by the donor's adult children who are the owners and beneficiaries of the policy. It makes sense that the donor gift money to the children to pay policy premiums.

-Any incidence of ownership in the policy by the donor results in loss of tax advantages.

-Done correctly, the children (or other beneficiaries) receive the death benefits at the death of the donor tax free. Since the donor has no right of ownership in the policy the proceeds are not included in the donor's estate for estate tax purposes. Note: while beneficiaries receive the death benefit income tax free, the death benefit is considered part of the policy owner's estate for estate tax purposes.

VIII. Managing the endowment fund.

Managing the congregation's endowment fund can be a potential source of conflict. The trust placed in those who are members of the fund's board is frequently questioned. Here are considerations for managing the fund.

1. Where to invest the money is a key question.
   -banks -- savings accounts, and certificates of deposit.
   -mutual funds.
   -individual securities (stocks and bonds).

2. The prudent person guideline can serve as a guide in determining where to invest the fund assets. The prudent person is representative of what a reasonable person would likely do given the same circumstance. This person would not take undue risk, yet would not be too conservative. A good way to think of this guideline is: Stick to basics, such as bank accounts, more conservative mutual funds, and blue chip stocks and investment grade bonds. Avoid small company stocks, junk bonds, derivatives, options, futures, and other investments with a higher risk.

3. Investments and board member skills and special knowledge need to be considered in managing the fund. On the one hand, do not get too sophisticated in investments based on one member's abilities. On the other hand, do not be afraid to go beyond the savings account and certificate of deposit offered by banks.

If the board is not comfortable with a proposed investment, or does not basically understand it, then avoid it. While being too conservative poses the risk of having returns that fail to keep up with inflation, being too aggressive in pursuit of high returns can also be hazardous to the fund's wealth. If something sounds too good to be true, it probably is. While well worn as a slogan, it brings a sound note of caution.

4. The question of in house versus custodial management arrangements are sure to arise. If the fund is relatively small and there is reasonable trust of the board members it makes sense to keep the management of fund assets in the hands of the board. Management fees charged by financial institutions, especially for smaller amounts of money, can be outrageously expensive.

Shop around for the best fees if a custodial arrangement is selected. Fees may be a percentage of fund assets, or a minimum flat fee, or a combination of fees. It may seem needless to mention, but stick with reputable established financial institutions and representatives.

5. Establish a procedure for reporting to the congregation. Regular reports are essential for maintaining trust that the fund is well managed, and they can be a way of keeping people informed about the fund. People want to know where the money is and where the money goes. If they do not have that knowledge provided to them they may harbor suspicions and not consider a possible donation to the fund.

6. Some people will give to the congregation. But some people like to give for specific ministries of the congregation, such as the music or educational ministry. If people have a specific interest they will be more attracted to give if they can specify that their gift be used to support a special ministry. The marketing potential of specific ministry gifts is important. The paperwork need not be too complicated.

Consider managing sub accounts of the endowment fund this way. Think of each dollar as a share of the fund. How many shares, dollars, are allocated for general purpose, music ministry, youth programs, outreach, and so forth? Determine the percent of each category. Allocate the total return of the fund's investments by percentage to each sub account.

IX. Use of professionals in the gift process.

When donors consider large gifts, insurance gifts, trust arrangements, and gifts designed to reduce estate taxes, various professionals become involved in the gift process.

Among the professionals that congregation endowment board members may encounter working with potential donors are:

- Attorneys
- Accountants
- Life insurance agents
- Financial planners
- Trust officers
- Stock and bond brokers
- Real estate agents.

Two things must be considered in working with these professionals. One, make sure the person is conversant in charitable giving. Some professionals are generalists. While they provide good service in many areas of their respective fields, they may not know the fine points of charitable giving. The tax consequences can be horrendous. Such disastrous results can sour donors on any kind of charitable giving in general and on their congregation in particular. The donors expect that board members will make sure the right questions are asked and that the fine points are covered.

Two, watch out for conflict of interest. An insurance agent makes money only when a policy is sold. Some policies provide larger commissions than others. Attorneys usually are paid a percentage of an estate as their fee for legal work. A potential donor considering a million dollar gift represents a potential $20,000 or $30.000 reduction in the attorney's income once the gift is removed from the donor's estate.

Another category of professional who can be a great source of help to a congregational endowment board is the development officer of a university, hospital, museum, or other nonprofit organization. Most of them would be glad to share their knowledge with the endowment board members. The best development people to contact are those working for larger institutions since they are more involved in the intricacies of charitable giving. Smaller organizations may limit their development position to annual fund drives or special event fund raising. Depending on their background such persons may or may not be helpful.

It might be helpful to meet with some of these professionals before the need arises. Insights gained from such conversations could be enlightening to endowment board members and give them confidence in their work.

X. Writing the by-laws (or articles of incorporation).

Include at least the following in the by-laws or corporate constitution:

- -The purpose of the fund, including the range of funding possibilities the board will consider.
- -Define the constituency of the board of trustees, including terms of office and limits on terms that can be served.
- -Establish investment policies.
- -Establish spending criteria and the process for decision making regarding what ministries will be funded.
- -Put in place the reporting requirements, what to include, and how often to report.

Conclusion.

A congregational endowment fund can be an exciting resource for financing congregational ministries. Its a way of making mission happen. It gives flesh and blood reality to a vision of God's coming kingdom. Money by itself is neither good nor bad. Its what money symbolizes for those who have it, give it, and receive it that makes a difference. Money given to a mission oriented congregtional endowment fund holds great potential, as an expression of the donor's faith, for the future of the congregation.

Appendix: Resources

Loren Mead, ENDOWED CONGREGATIONS: PROS AND CONS. Published by The Alban Institute as an on demand report.

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